

CHAPTER 14: MANAGEMENT AND DISPOSAL OF REO PROPERTY

14.1 INTRODUCTION

When the Agency takes ownership of a project, adding the property to its inventory through liquidation proceedings, the project becomes real estate owned (REO). When the title transfers to the Agency, the property becomes an Agency asset. The Agency's objectives in managing and selling its inventory of REO properties include:

- Preserving affordable, decent, safe, and sanitary housing for tenants or potential tenants;
- Maintaining the value of the housing project;
- Protecting the Agency's financial interests;
- Ensuring that the properties comply with state and local code requirements and applicable environmental regulations; and
- Ensuring compliance with environmental requirements.

14.2 OVERVIEW OF THE CHAPTER

The chapter is divided into five sections.

- Section 1 describes the management of custodial and REO property. It describes acceptable management methods; discusses issues related to taking possession of custodial and REO properties, such as disposing of non-security property and paying taxes and insurance premiums; and explains requirements related to maintenance, environmental concerns, and other management issues.
- Section 2 covers the disposition of REO property. It describes the methods for pricing and selling the properties and outlines procedures for accepting bids from potential purchasers. It also describes the standards the property must meet before being sold.
- Section 3 describes the environmental requirements that must be fulfilled before selling an REO property. These include requirements related to flood and mudslide hazard areas, wetlands, coastal barrier resource systems, historic places, protective covenants and easements, underground storage tanks, and hazardous substances.
- Section 4 outlines the procedures for processing and closing the sale of an REO property. These procedures are similar to the procedures for closing other Agency loans. This section also highlights some of the special considerations for REO properties.
- Section 5 provides instructions on processing credit sales for non-program terms.

SECTION 1: MANAGEMENT OF CUSTODIAL AND REO PROPERTY

14.3 OVERVIEW OF THE SECTION

The Agency assumes management responsibility for two types of properties: custodial and real estate owned (REO). Custodial property is borrower-owned property which has been abandoned. REO is Agency-owned property to which the Agency has acquired title, either as a result of foreclosure or conveyance by deed in lieu of foreclosure. This section outlines the requirements for management of each type of property.

Servicing officials are responsible for ensuring that custodial and REO properties are appropriately managed and maintained. The goal of property management is to protect tenants and the interests of the government. Consequently, Agency efforts to secure and manage these properties are to begin immediately once the following occurs:

- The property title is conveyed to the Agency; or
- The Agency determines property is abandoned.

14.4 MANAGEMENT METHODS AND CONTRACTS

The Agency has the authority to contract with qualified management entities to perform the management activities discussed in this section. The extent of management is dependent on factors such as:

- The nature of the project;
- The project's location;
- The condition of the project;
- Necessary maintenance; and
- Availability of acceptable management entities.

In some cases, the existing management agent can be maintained; in others, the Agency must hire a new management agent to provide all property management services on behalf of the Agency.

A. Selecting a Management Contractor

Management contractors are selected in accordance with Agency procurement procedures outlined in RD Instruction 2024-A, Acquisition, Sales, and Leasing Authority. Alternative methods for selecting a management contractor may be established by the Agency if it is in the best interest of the government. Alternative selection methods require advice from the OGC. Prior to obtaining a management agent for custodial property, the Agency should determine if court approval is required.

B. Management Contract Requirements

At a minimum, management contracts must:

- Allow for properties to be added or removed from the contractor's assignment, whenever necessary, such as when a property is taken into custody, acquired, or sold during the period of a contract;
- Prohibit the contractor or associates of the contractor from performing repairs if the executed agreement calls for the contractor to provide detailed repair specifications;
- Require the management agent to hold security deposits in trust and handle them in accordance with the tenant's lease or occupancy agreement;
- Include covenants requiring compliance with environmental laws.

The management agent must develop an Affirmative Fair Housing Marketing Plan (AFHMP), in accordance with RD Instruction 1901-E, Civil Rights Compliance Requirements. The AFHMP must be submitted to the loan office. The AFHMP must receive written approval from the Civil Rights Coordinator in the Rural Development State Office. A sample statement of work for a project management contract is provided as **Attachment 14-A**.

C. Management Costs

The costs of management services related to REO property will be paid out of income generated by the housing project being managed. If income from the housing project is inadequate to pay for management services, Agency resources may be used to pay for management services.

D. Project Funds

When a property becomes REO, the Agency transmits operating and maintenance, reserve accounts, and escrow funds to the Finance Office. The former borrower's account is credited for these amounts. If there is a surplus of funds, the Finance Office will forward a refund check payable to the former borrower.

14.5 TAKING POSSESSION

A. Taking Custodial Possession

The Agency is authorized to take custody of security property when a borrower becomes incapacitated, dies, or has abandoned a security property. When the Field Office has attempted for more than 30 days, and is unable to contact a borrower, the Loan Servicer must inspect the property to determine its status and to attempt to locate and contact the borrower. The Field Office should seek the advice of OGC in making its determination and recommendation.

1. Determining Whether A Property Has Been Abandoned

The determination that a property has been abandoned requires significant investigation and documentation. In addition to the actions described in this paragraph, field staff must follow any procedures required by state or local law in order to confirm the determination of abandonment and to take custodial possession. The Agency cannot act to obtain possession of a property as long as a lien holder has legal possession of the property, or the borrower or the lien holder has a right to lease proceeds. Field staff cannot classify a property as “abandoned” prior to documenting attempts to:

- Determine that there is no clear evidence of management presence at the project. For example, a site visit indicates that tenants are unable to contact borrower or property manager regarding repairs or rent collection, the project has fallen into disrepair due to a total lack of maintenance activities, or the Loan Servicer cannot locate the borrower or property manager;
- Locate the borrower through sources including, but not limited to, tenants, the postal service, utility companies, business associates, relatives, insurance agents, and tax authorities;
- Determine whether there are other liens on the property. If liens exist, whether the lien holder(s) are willing to work with the Agency to secure the property.

2. Recommendation for Taking Custody

The Field Office will report its findings to the State Director. The report will recommend that a property be taken into custodial possession if it appears that the property has been completely abandoned and the Agency needs to assume responsibility for it in order to protect the security. Alternatively, if the Field Office reports that the property is occupied the report will give details as to whether the occupants are under a lease or are unauthorized. The Field Office will provide any other relevant details and recommend future action. When appropriate, the State Director will authorize the Field Office to take custodial possession. When the Field Office believes that a property is abandoned, it must prepare a report, which provides evidence of a property’s abandonment. The report is placed in the borrower’s case file and a copy of the report is forwarded to the State Office.

3. Liquidation

The need to take custodial possession of a property may occur before or after a loan has been accelerated. If liquidation is not already in progress, taking custodial possession should initiate the process. Field staff are responsible for conducting liquidation activities.

B. Acquisition of an REO Property

When a Field Office acquires a property, field staff must notify the State Director. An additional REO case file should be created from the original case. The REO case file

should include the property title, recent inspection reports, appraisals, environmental reviews, and any other documentation related to the physical condition or value of the property. No information related to the borrower is needed in the REO file.

14.6 INSPECTING AND SECURING CUSTODIAL AND REO PROPERTY

Once REO property is acquired, field staff must inspect the property to determine what steps need to be taken to further ensure its security and maintain its value. The inspection will allow field staff to designate the property as program or non-program and evaluate the need for repairs.

A. Inspecting and Classifying the Property

Field staff must perform an on-site field inspection of REO property to:

- Determine repair needs;
- Gather information to assist in completing the environmental review;
- Assist in updating the due diligence report and appraisal, as necessary; and
- Take necessary actions to secure and maintain the housing project.

Based on the results of the inspection, field staff designate REO property as program or non-program property after considering factors such as size, design, possible health and/or safety hazards, and obsolescence due to functional, economic, or locational conditions. REO property may be sold as non-program property if any of the following conditions exist:

- The housing project does not meet Agency requirements and the cost of bringing the housing into compliance is determined, by the Agency, to be economically unfeasible based on the amount of funds available to the Agency and the housing needs in the market area where the housing is located.
- Attempting to sell the property on program terms is not in the best interest of the federal government.
- Hazardous substances or petroleum products have been released on the property and the cost of clean-up is estimated to exceed the dollar value the Agency will recover through sale of the property.

REO property in an area no longer designated rural is treated as if it were still in a rural area.

B. Securing Custodial and REO Property

When the Field Office assumes management responsibility and takes possession of REO or custodial property, immediate steps must be taken to inspect and secure the property whether by Field Office staff or management contractor.

1. Physical Security of Vacant Properties

If the property is vacant, it should be locked or otherwise secured and a no trespassing notice should be posted. For REO only, after an inspection determines utility systems are in safe operable condition, utility companies should be contacted to maintain or reinstate utility service. An inventory should be made of any non-security personal property left on the premises and efforts made to identify any owners or lien holders.

2. REO Properties Occupied By Tenants

REO property may be occupied by tenants with leases executed by the former borrower. The Agency may require tenants to sign a new lease, but if it is in the interest of the Government, the Agency may honor existing leases. The Agency may evict unauthorized tenants.

When units in an REO property are under an existing lease and the Agency decides to continue the lease, the tenant must be notified, in writing, that the Agency has acquired the former owner's rights under the lease and that all payments should be remitted to the Agency's management agent. If a lease is to be terminated, the tenant must be notified, in writing, that their lease is being terminated in 30 days, and they must vacate. The Office of General Counsel (OGC) should be contacted for advice and assistance prior to evicting a tenant in order to obtain possession of an REO property.

Rent payments due and payable before the date the Agency acquired the property are applied to the borrower's account. Any surplus funds will remain with the project.

14.7 DISPOSITION OF NON-SECURITY PROPERTY

The Agency has no legal claim to any non-security, owner or tenant property left on the premises. State or local law may affect procedures for disposing of personal property left on the premises of an REO or custodial property. Field staff must comply with any state or local requirements, as well as the procedures discussed in this paragraph. If the owners or lien holders of any personal property that remains custodial or REO property can be identified and located, field staff must offer them a reasonable opportunity to remove the property. Any conversations with the owner of the property should be documented and placed in the case file.

A. Custodial Property

The Agency may remove any non-security personal property from custodial properties as long as such property can be safely stored. Personal property cannot be removed and stored if:

- The storage facility presents a hazard to the security of the property, such as a leaking roof or unsecured area which allows access to the property by unauthorized persons.
- The personal property itself presents a hazard, such as flammables or explosives. Hazardous materials must be managed in compliance with Section 14.10 of this chapter.

B. REO Property

1. Notice to Owners or Lien Holders of Personal Property

If the property is not retrieved after the initial notification, a certified letter should be sent, return receipt requested, notifying the owner or lien holder of the date on which the Agency will dispose of the property, and that the property may be retrieved before the disposition upon payment of any expenses incurred by the Agency related to the personal property, such as advertisement or storage.

2. Disposal of Unclaimed Property

The Field Office will dispose of unclaimed property in accordance with its value and conforming with local practices. For example, if there are items of significant value, an advertisement may be placed in the local newspaper. Unclaimed tenant property will be disposed of in accordance with the terms of the lease.

3. Income from Disposition

Proceeds from the sale of items under lien should be paid to any owner or lien holder after deducting Agency selling expenses. If there is no known owner or lien holder, proceeds are applied to the REO account.

14.8 TAXES AND INSURANCE

A. Taxes

REO property is subject to taxation by state and local political jurisdictions in the same manner and to the same extent as other properties, unless state law specifically exempts property owned by the federal government. If a jurisdiction changes the law to begin taxing government-owned property, only taxes accruing after the effective date of the change will be paid. Field staff must notify the taxing authority, in writing, when title to real estate is acquired and provide the Field Office address to which tax bills should be sent during Agency ownership.

If the value of the property is significantly less than the value at which it is being taxed, as soon as it is acquired, the Agency may request a new assessment by the local taxing authority. Management contracts between the Agency and property managers may include provisions allowing the management agent to request a new tax assessment.

If property is acquired subject to a prior lien, before the Agency pays taxes, field staff must contact the prior lien holder to determine if that lien holder will pay the taxes.

Taxes on program property are paid when due. Taxes on non-program property may be deferred until the property is sold if the taxes that accrue before disposition exceed the value of the property. If the taxing authority schedules a tax sale before the Agency can sell the property, field staff will determine what is in best interest of the government. To make this determination the field staff will calculate the net recovery value that would result from paying the taxes and continuing sales efforts. This calculation will be compared to the net recovery value if the Agency allowed the property to be sold for delinquent taxes. (See Chapter 12 for a more detailed discussion of net recovery value.)

B. Insurance

1. Custodial Property

Insurance on custodial property will be maintained per program instructions.

2. REO Property

Insurance will not be canceled when property is acquired. However, the Agency will pay additional premiums to continue coverage only when it is in the best interest of the federal government. If it is necessary to file a claim, field staff should submit the claim and direct that insurance proceeds be forwarded to the Finance Office.

14.9 ENVIRONMENTAL REQUIREMENTS

The Agency must complete the appropriate level of environmental review under the National Environmental Policy Act for proposed management activities involving custodial and REO properties in accordance with RD Instruction 1940-G, Environmental Program. Management activities subject to environmental review include repair and maintenance activities as well as leasing of custodial and REO property.

Repair and maintenance activities will normally qualify as categorical exclusions provided the proposed action will not alter the purpose, operation, location, or design of the project as originally approved. Leasing of custodial and REO property will normally qualify as a categorical exclusion provided the proposed action is not controversial for environmental reasons and will not result in a change in use of the property in the reasonably foreseeable future. If such criteria cannot be met, refer to RD Instruction 1940-G, Environmental Program, for further direction.

When certain environmental resources are present or when certain conditions exist, specific limitations or constraints are imposed by environmental law on the Agency's repair and maintenance activities and leasing activities. In such cases, an Environmental Assessment (EA) may be required to address the situation properly. Consultation with the State Environmental Coordinator is recommended before proceeding in the following circumstances.

A. Repair and Maintenance Activities

1. Coastal Barrier Resources System (CBRS)

Any action proposed to be taken on a custodial or REO property within a CBRS must be coordinated with the State Environmental Coordinator and the Regional Director of the U.S. Fish and Wildlife Service (USFWS). In emergency situations to prevent imminent loss of life, imminent substantial damage to the inventory property, or the disruption of utility services, minimum steps necessary to prevent such loss or damage may be taken without first consulting the USFWS as long as the Regional Director of the Service is immediately notified of the emergency action taken.

Maintenance or repair is prohibited for property located within a CBRS if:

- The action goes beyond maintenance, replacement-in-kind, reconstruction, or repair and would result in the expansion of any roads, structures or facilities;
- The action is inconsistent with the purposes of the Coastal Barrier Resources Act (CBRA); or
- The property to be repaired or maintained was initially the subject of a financial transaction that violated the CBRA.

The Administrator should be asked to review any cases where the Agency and the USFWS disagree on the effect of a plan of action or where otherwise prohibited maintenance and repair must be undertaken. Approval for action will not be granted unless the Administrator determines, through consultation with the Department of Interior, that the proposed action does not violate the provisions of the CBRA.

2. Historic and Archaeological Resources

Properties that are listed or eligible for listing on the National Register of Historic Places, in whole or in part, will be repaired as necessary to protect their historic integrity after consultation with the State Historic Preservation Officer (SHPO) and the Advisory Council on Historic Preservation. If a property is listed or eligible for listing on the Register and also is located within the CBRS, the property cannot be repaired without the prior approval of the USFWS.

field staff will review the current Register to determine if the property is listed. If the property is not listed, the field staff will consult with the SHPO when the property is considered potentially eligible for the Register. A property is considered potentially eligible if it contains a structure more than 50 years of age or, regardless of age, if the property is known to be of historic or archaeological importance, or has apparent significant architectural features.

3. Floodplains and Wetlands

If the Agency is considering a substantial improvement or repair to custodial or REO property located in a flood plain or wetland, the Agency must first consider whether there are practicable alternatives to such further investment in the floodplain or wetland area. For example:

- Could the property be sold “as is” with notice of floodplain/wetland hazard?
- Could the property be sold “as is” with a requirement that the structure be removed from the site?
- Could the Agency remove the structure first and sell the land with notice of hazard?

If there are no practical alternatives to the substantial improvements, then the Agency may proceed with the improvements, provided it includes any practical mitigation measures. On an existing structure, mitigation will generally involve some form of floodproofing, such as elevating hot water tanks, or heating and ventilation units.

A substantial improvement is defined as any improvement the cost of which equals or exceeds 50 percent of the market value of the structure either (1) before the repair is started, or (2) if the structure has been damaged, before the damage occurred. The cost of compliance with health, sanitary, and safety codes is not included in the calculation of the substantial improvement cost, nor is the cost of repair to an historic structure included. If the repairs do not qualify as substantial, the Agency does not need to search for alternatives or mitigation measures.

4. Reportable Underground Storage Tanks

Properties that contain certain types of underground storage tanks must be reported to the state agency identified by the Environmental Protection Agency (EPA) within 30 days of Agency acquisition. **Attachment 14-B** provides a list of those underground storage tanks which must be reported, and those which are exempt from reporting requirements. A State Supplement will be provided on a case-by-case basis with the necessary EPA forms or acceptable state forms that may be used to accomplish the reporting, as well as detailing any additional state reporting requirements. A copy of the report must be maintained in the REO file, and any prospective buyers of the property must be furnished with a copy of the report.

B. Lease or Management Contract

1. Historic and Archaeological Resources

A property that is listed or eligible for listing on the National Register of Historic Places may be leased or operated by management contract only after the Agency and the SHPO determine that the lease or contract will adequately ensure the property’s condition and historic character.

2. Floodplains and Wetlands

Before executing a lease for a property containing wetlands or located in a special flood or mudslide hazard area identified by the Federal Insurance Administration, field staff must provide written notice of the hazard to the lessee. The notice must be attached to the lease. Any management contract must require the contractor to fulfill this obligation.

The lease or management contract for custodial or REO property containing wetlands or located in a floodplain area will also specify any uses of the property by the lessee or tenant that are restricted under any federal, state or local floodplain and wetland regulations, as well as other appropriate restrictions. Examples of use restrictions would include prohibition of draining or filling of floodplain or wetland areas, and prohibitions of new above-ground construction on the portion of the property located in the floodplain or wetland area.

3. Environmental Requirements for Leasing

All property considered for lease must be evaluated for possible hazardous substance contamination. To do this, the field staff completes the *Transaction Screen Questionnaire, ASTM Standard E-1528 (TSQ)*, the initial level of inquiry in the due diligence process. (If a TSQ was completed prior to acquisition of the property, the Loan Approval Official must determine if the TSQ should be updated.) If the completed or updated TSQ indicates potential contamination, it will be sent promptly to the State Environmental Coordinator for further evaluation and guidance. All clean-up actions if appropriate, will be taken under the guidance of the State Environmental Coordinator.

When leasing REO property, in whole or part, field staff must in all cases, notify potential lessees of the risk for potential contamination from hazardous substances, hazardous wastes, or petroleum products by providing the lessee with a copy of the Agency's due diligence report on the property. The due diligence report should be accompanied by a written disclaimer to the effect that the Agency does not provide any guarantee as to the accuracy of the report, but is simply making the results of its inquiry available to the interested public.

14.10 MANAGEMENT OF HAZARDOUS SUBSTANCES

The Agency will reasonably and prudently attempt to minimize its liability under hazardous substance and hazardous waste laws. Diligent efforts will be made to evaluate economic risks to real estate posed by the presence of contamination from hazardous substances, hazardous wastes, and petroleum products, including underground storage tanks. If a release or threatened release of hazardous substances, hazardous wastes or petroleum products on abandoned, custodial, or Agency owned property poses an imminent and substantial threat to human health and the environment, the Agency will notify the appropriate environmental regulatory authority and will take emergency response actions under the guidance of that authority.

The elements of potential liability and economic risk are addressed by the Agency by performing due diligence. Due diligence is the process of inquiring into the environmental condition of real estate in the context of a real estate transaction to determine the presence of contamination from hazardous substances, hazardous wastes, and petroleum products, and what impact such contamination may have on the market value of the property.

The field staff initiate due diligence by completing the *Transaction Screen Questionnaire, ASTM Standard E-1528 (TSQ)*, the initial level of inquiry in the due diligence process. If the completed TSQ indicates a potential for contamination, it will be sent promptly to the State Environmental Coordinator for further evaluation and guidance.

For all servicing actions that require a determination of market value, the appropriate level of due diligence will be performed in conjunction with the appraisal. Due diligence also must be performed in conjunction with any servicing action that may lead to acquisition of security property.

The field staff should be aware of suspicious situations during security inspections of custodial and REO property. If unauthorized dumping of potentially hazardous material is noted, due diligence will be performed.

To minimize the Agency's liability, any response action taken by the Agency in responding to a release or threatened release of hazardous substances or petroleum products on inventory property will be taken in consultation with and at the recommendation of the appropriate environmental regulatory authority. In the case of custodial property, the State Environmental Coordinator may initiate, as necessary, limited emergency response actions to stabilize an emergency or imminent and substantial threat to human health and the environment.

If the Agency is notified or made aware of the presence of an underground storage tank on custodial or REO property, field staff must ensure that the tank complies with appropriate environmental regulatory authority requirements or is removed. When reinstalling a fuel storage system, aboveground storage tanks should be used where feasible.

Field staff must complete or update a TSQ to document the existing environmental conditions at the property prior to leasing inventory property.

14.11 PHYSICAL MAINTENANCE AND REPAIR

Custodial property will be maintained and repaired only as needed to protect the security of the property and to prevent deterioration. In the event of damage or theft, the procedures described under paragraph A below should be followed.

REO property designated to be sold as program property must be repaired, as necessary to meet the Agency's requirements for decent, safe, and sanitary housing.

REO property designated to be sold as non-program property will be managed in a manner which:

- Removes health and safety hazards;

- Prevents deterioration; and
- Complies with state and local requirements for the sale of the property.

Additional repairs or renovations will only be made if they will enhance the sale value of the property and are determined, by the Agency, to be in the best interest of the government.

A. Vandalism and Theft

Field staff will report any willful damage or theft to the local law enforcement authorities and in whatever manner necessary, to attempt to resolve the incident, including signing complaints and testifying at hearings or trials.

Field staff should send a written report of the incident to the State Director and a copy to the Regional Office of Inspector General (OIG). The State Director, in consultation with the OGC as necessary, will advise and assist the field staff.

Damage to REO program property as a result of vandalism and theft may be repaired as necessary to continue marketing. Repairs may include cost-effective improvements to minimize the likelihood of future damage, such as increased lighting, security fencing, and removal of shrubs that limit visibility. Non-program property should be broom swept, but generally will not be repaired unless necessary to prevent deterioration. Custodial property should be repaired only to protect the security and to prevent deterioration.

B. Off-Site Repairs or Improvements

The Agency may require off-site repairs or improvements to protect property from damage, to protect the government's interest, or to enhance the marketability of property. Off-site improvements must be approved by the State Office. To obtain approval, field staff must prepare a justification that demonstrates failure to make the improvements would likely result in a loss in property net recovery value greater than the expenditure, and that there are no other feasible means with state or local entities to accomplish the same result.

To obtain off-site improvements, the Agency may enter into a contract with a private company or enter into a cooperative agreement with a state or local government, or other entity to obtain repairs or improvements. Under a cooperative agreement, the entity will provide money, property, services, or other items of value to the entity to accomplish a public purpose. While cooperative agreements are not a contract action, the authority, responsibility, and administration of a cooperative agreement must be consistent with contract action. The OGC should be consulted when a cooperative agreement is considered.

C. Lead-Based Paint

The property must be managed in a manner consistent with RD Instruction 1940-G, Environmental Program.

1. Control of Lead-Based Paint Hazards

To control lead-based paint hazards, the Agency must ensure that painted surfaces in the property are intact. Surfaces that are not intact must be repaired in a lead-safe manner.

2. Disclosure

The Act requires lessors of housing built before 1978 who receive federal assistance to provide the lessees with information about the housing's lead history and general information on lead exposure prevention. Under the disclosure rules, before the lessee becomes obligated under any contract to lease the housing, field staff must:

- Provide the lessee with the lead hazard information pamphlet, *Protect Your Family from Lead in Your Home*, available from the National Lead Information Clearinghouse at 1-800-424-LEAD, or a similar EPA-approved pamphlet developed by the state; and
- Disclose the presence of known lead-based paint and/or lead-based hazards in such housing and provide the lessee with any lead hazard evaluation report available to the Agency.

14.12 SPECIAL USES OF REO

A. Transitional Housing for the Homeless

By a Memorandum of Understanding between the Agency and the Department of Health and Human Services, REO property that is not under lease or sales agreement may be leased to public bodies and nonprofit organizations to provide transitional housing for the homeless. (See **Attachment 14-C**.)

B. Use by Federal Emergency Management Agency (FEMA)

By a Memorandum of Understanding between the Agency and FEMA, REO property which is not under lease or sales agreement is available to shelter disaster victims in an area designated as a major disaster area by the President. In such an event, FEMA assumes responsibility for all costs associated with inhabiting the dwelling.

FEMA and the Agency must sign a "Letter of Assignment," which includes a mutually agreed upon inspection report outlining the condition of the property being assigned to FEMA. Field staff should retain the Letter of Assignment in the REO file. No rent is paid by FEMA for the first 12 months from the date of the letter of assignment of the housing. Beyond that, FEMA pays the monthly fair market rental value as determined by the Agency.

See **Attachment 14-D** for the Memorandum of Understanding and Letter of Assignment.

C. Mineral Leases

When it is in the best interest of the government, the Agency may lease mineral rights associated with REO property. OGC should be contacted for assistance in preparing the lease agreement. The appropriate level of environmental review must be completed prior to any agreement to lease mineral rights. Since such actions may be controversial and may have the potential for significant impact on the environment, prior consultation with the State Environmental Coordinator is required.

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SECTION 2: DISPOSITION OF REO PROPERTY [7 CFR 3560.503]

14.13 OVERVIEW OF THE SECTION

The Agency will make every effort to sell real estate owned (REO) properties quickly and at the best possible price. Whenever possible, preference will be given to selling REO program property to a program borrower.

A. Sale Methods and Pricing

Most REO properties are sold through public drawing. However, the Agency may sell properties through auction, sealed bid, negotiation, or agreements with other federal agencies, such as the Department of Housing and Urban Development (HUD).

REO properties are initially priced for sale at their present market value, as determined by appraisal. Administrative price reductions may be taken over time to facilitate sale of the property (see paragraph 14.14 for a discussion of price reduction). A schedule is published that restricts sales of program property to program-eligible buyers for a period of time before any offering to the general public, and whenever there is a reduction in price.

An Affirmative Fair Housing Marketing Plan, as described in Paragraph 14.15, must be prepared for REO multi-family properties of four or more units.

B. Financing

When funds are available, the Agency may offer financing to buyers of REO property. When program credit is offered, the loan is processed following the procedures described in the Loan Origination Handbook.

Non-program credit terms are offered when the buyer is not eligible for a Section 514 or 515 loan, or the property does not qualify as a program property. Section 5 provides instructions for credit sales on non-program terms. Buyers who receive financing on non-program terms must be advised that they are not eligible for interest credit or rental assistance.

C. Warranty

The Agency does not provide a warranty of either the title or the physical condition of any REO property.

14.14 PRICING AND SALES SCHEDULES

REO housing is priced and initially offered for sale at its present market value, based on a current appraisal. Administrative price reductions may reduce the offering price to facilitate the sale. Mineral, water, and similar rights are generally sold with the property and are not sold separately except when the government's security interest will not be jeopardized. Lease or royalty interests that do not pass by deed are assigned to the buyer.

A. Appraisals

To determine the property's present market value, the Field Office must arrange for an appraisal in accordance with the procedures described in Chapter 3, Property Requirements, of the Loan Origination Handbook. If repair or improvement is planned, the appraisal must provide both as-is and as-improved values. Each as-improved appraisal must include a list of the planned repairs. Any special flood or mudslide hazard areas or wetlands and related use restrictions must be reflected in the appraisal. All REO property considered for disposal or lease must be evaluated for possible contamination from hazardous substances or petroleum products through the process of due diligence and completion of the *Transaction Screen Questionnaire, ASTM Standard E-1528 (TSQ)* as described in paragraph 14.29. This will normally be completed at the same time as the appraisal.

A property must be reappraised whenever its condition has deteriorated, it has been significantly damaged or vandalized, additional repairs and improvements have been made, or there has been a change in market conditions. Field staff should be especially alert to potential contamination from unauthorized dumping while the property is owned by the Agency and, if necessary, update the TSQ and the appraisal prior to sale or lease. The need for reappraisal should be established as quickly as possible so that the property is offered at its true value. Appraised value is not affected by administrative price reductions.

B. Sales Schedules and Administrative Price Reductions

The sale of REO program property is restricted to program-eligible buyers when a property is offered for sale and any time an administrative price reduction is taken. Exhibit 14-1 provides the sales schedule for program property. The sales price is fixed when a sales contract is executed and does not decrease further based upon scheduled price reductions.

Exhibit 14-1

Sales Schedule for Multi-family Housing REO Property Program Property

Days from Initial Offer	Action
Day 1	Initial offer (appraised as-is value with subsidy).
Day 45	If no acceptable offer, reduce price by 10 percent and offer again.
Day 91	If no acceptable offer, reduce price by another 10 percent or use other methods (additional 10 percent price reductions allowable after 45 days)
Day 180	If no acceptable offer, submit REO file with documentation of marketing efforts to State Office for further advice on sales incentives or to authorize sealed bid/auction. Loan Servicer may reevaluate whether the project should be classified as a program property.

Exhibit 14-2 provides the sales schedule for non-program properties. If a program property has not sold following active marketing efforts and two price reductions, field staff will reevaluate the property to determination if it should continue to be marketed as a program property. The reevaluation process may include an updated appraisal.

Exhibit 14-2

Sales Schedule for Non-Program REO Property

Days from Initial Offer	Action
Day 1	Initial offer (appraised as-is value without subsidy).
Day 45	If no offer, reduce price by 10 percent and offer again. Additional 10 percent price reductions are allowable after 45 days.
Day 91	If no acceptable offer, reduce the price by another 10 percent or use other sale methods.
Day 180	Submit REO file with documentation of marketing efforts to State Office for further advice on sales initiatives to authorize sealed bid/auction.

14.15 MARKETING AND ADVERTISEMENT

A good marketing plan is the key to reaching the maximum number of potential buyers and to ensuring that eligible program applicants have an opportunity to purchase REO properties. The Agency may advertise directly or contract for advertising services. Broker contracts may include advertising services. All advertisements must state occupancy or environmental restrictions.

A. Fair Housing and Affirmative Fair Housing Marketing Plan

All advertising must meet equal housing opportunity requirements and contain the equal housing opportunity statement and logo.

B. Truth in Lending Requirements

If the availability of Agency financing will be advertised, marketing efforts must conform to the requirements of the Truth in Lending Act . Exhibit 14-3 highlights these requirements (see RD Instruction 1940-I, Truth in Lending—Real Estate Settlement Procedures, for additional information).

Exhibit 14-3

Truth in Lending Highlights

- Advertisements that state specific credit terms must state only terms that will actually be offered.
- Any finance charge listed must be stated as an annual percentage rate.
- Key terms related to financing used in the advertisement must be defined

C. Advertising and Marketing Methods

Advertising efforts should be designed to reach a broad audience. Each Field Office should identify appropriate marketing efforts and tailor them for each market area. At a minimum, advertisements must be placed in newspapers of general circulation and posted on the Field Office bulletin board. Other marketing efforts that may be appropriate include:

- Posting advertisements in public locations accessible to prospective purchasers, including community bulletin boards and major employment sites;
- Broadcasting announcements on radio or television; or
- Informing potential program applicants or investors of the availability of REO properties.

Advertisements must include the following:

- Appropriate language, stressing the need for potential buyers to complete and submit an application and other required documentation;
- Any restrictive use requirements that will be attached to the project and added to the property's title;
- Sale price; and
- Date, time, and location of drawing. The date and time must allow adequate time for advertising and review of application packages.

D. Review of Marketing for Unsold Properties

At least quarterly, the State Director must review the status of unsold REO property to ensure that acquired properties are being placed on the market promptly, properties on the market are selling within a reasonable time frame, and that properties under contract are closed in a timely manner. Of particular concern are:

- Properties acquired more than 90 days ago that have not yet been made available for sale;
- Program properties that have been available for sale for 6 months or more and are not under contract;
- Non-program properties that have been available for sale for 4 months or more and are not under contract; and
- Properties that have been under contract for more than 60 days, and have not closed.

14.16 SPECIAL MARKETING TECHNIQUES

A. Buyer Incentives

The State Director may authorize buyer incentives when field staff provide evidence that a specific market area is depressed and the incentives are required to stimulate buyer interest. To request approval for buyer incentives, the Field Office must describe past efforts to sell the property and explain why the proposed incentives are expected to produce improved results. Incentives, such as the payment of closing costs, may be appropriate for any property. Amortization schedules longer than the standard term may be offered for non-program properties.

B. Broker Incentives

When an additional broker incentive is needed, such as when a very low-value property offers an inadequate commission, the State Director may authorize a minimum commission or fixed-amount sale bonus. To request the incentive, the Field Office must describe the past efforts to sell the property and justify the amount and the purpose of the incentive. Upon the approval of the State Director, a written offer of the incentive that specifies the requirements and circumstances in which the incentive will be given must be provided to the broker.

C. Acquisition of Land, Easements, or Rights-of-Way to Effect Sale

When it will help the sale of REO property and it is in the best interest of the Government, the State Director may authorize the acquisition of adjacent land, easements, or rights-of-way in order to cure title defects or encroachments. Additional land may not be acquired at a cost in excess of its appraised market value.

14.17 REO PROPERTY NOT MEETING PHYSICAL STANDARDS

When REO property does not meet the Agency's dwelling standards, and making repairs that will allow the property to meet these standards is not economically feasible for the Government, the property is listed, advertised, and sold with specific occupancy restrictions.

Housing that does not meet the Agency's dwelling standards may still be considered decent, safe and sanitary if it:

- Is structurally sound and habitable;
- Has a potable water supply;
- Has functionally adequate, safe, and operable heating, plumbing, electrical, and sewage disposal systems;
- Meets the Agency's Thermal Performance Standards; and

- Is safe—that is, a hazard does not exist that would endanger the health or safety of occupants.

The deed by which such a property is conveyed will contain a covenant restricting the new owner from allowing occupancy of affected residential units until it those units meet the Agency’s dwelling standards, as discussed in Chapter 3, Property Requirement, of the Loan Origination Handbook. Property that is not decent, safe, and sanitary must still meet the Agency’s environmental requirements, including the management of hazardous substance requirements discussed in paragraph 14.10.

In the event that the Agency has acquired property that is unsafe and cannot feasibly be made safe, for reasons that are environmental in nature or relate to contamination from hazardous substances or petroleum products, field staff will provide appropriate information to the State Director including the observations and recommendations of the State Environmental Coordinator. The State Director will submit the case file, along with complete documentation of the problem and a recommended course of action, to the Deputy Administrator, Multi-Family Housing, with a copy to the Director, Program Support Staff, for their joint review and guidance.

A. Notice of Occupancy Restriction

The notice of sale and sale contract must describe the specific conditions that prohibit occupancy and the items necessary for the property to meet decent, safe, and sanitary standards, using *Form RD 1955-44, Notice of Residential Occupancy Restriction*, or language similar to the following:

“Pursuant to Section 510(e) of the Housing Act of 1949, as amended, 42 U.S.C. 1480, RHS has determined dwelling unit or units on this property inadequate for residential occupancy. The quitclaim deed by which this property will be conveyed will contain a covenant excluding the inadequate residential unit(s) from residential use until the dwelling unit(s) is repaired or renovated as follows:” (insert the items necessary for the property to meet decent, safe, and sanitary standards, clearly indicating the inadequate unit(s) and necessary repairs for each unit.)

For purposes of advertising, the list of specifications may be replaced with a statement to contact the Agency, or the real estate broker under an exclusive listing contract or “any real estate broker” for open listing agreements, whichever is relevant, for a list of specific items necessary for the property to meet decent, safe, and sanitary standards.

B. Quitclaim Deed Restrictive Covenant

The quitclaim deed must contain a covenant restricting residential occupancy if units within the project fail to meet the Agency’s dwelling standards. The covenant must describe the conditions which prohibit occupancy of specific units and specify the improvements that are necessary for the property to fully comply with Agency standards

for housing that is decent, safe, and sanitary. The covenant may use *Form RD 1955-44, Notice of Residential Occupancy Restriction*, or language in a State Supplement, similar to the following:

“Pursuant to Section 510(e) of the Housing Act of 1949, as amended, 42 U.S.C. 1480, the purchaser (‘Grantee’ herein) of the above described property (‘subject property’ herein) covenants and agrees with the United States acting by and through the U.S. Department of Agriculture (‘Grantor’ herein) that the inadequate dwelling unit(s) located on the subject property as of the date of this quitclaim deed will not be occupied or used for residential purposes until the item(s) listed at the end of this paragraph have been accomplished. This covenant shall be binding on Grantee and Grantee’s heirs, assigns, and successors and will be construed as both a covenant running with the subject property and as equitable servitude. This covenant will be enforceable by the United States in any court of competent jurisdiction. When the existing dwelling unit(s) on the subject property complies with the aforementioned standards of the U.S. Department of Agriculture in accordance with its regulations, the subject property may be released from the effect of this covenant and the covenant will thereafter be of no further force or effect. The property must be repaired as follows:_____.” (Insert the items referenced in the notice of sale and sale contract, necessary for the property to meet decent, safe, and sanitary standards.)

C. Release of Restrictive Covenant

When the owner requests a release of the restrictive covenant, the Agency inspects the property. The Agency will release the covenant if the conditions which prohibited occupancy have been corrected, the specific items necessary for the property to meet decent, safe, and sanitary standards have been provided, or the structure necessitating the restrictive covenant has been removed from the site. Restrictive covenants, established as environmental mitigation measures, will not be released without the concurrence of the State Environmental Coordinator.

14.18 DISPOSITION BY PUBLIC DRAWING

Public drawing is the preferred and most common method of sale for REO properties. Exhibit 14-4 outlines the public drawing process. Use of any other sale method requires approval from the State Office.

Exhibit 14-4**The Disposition by Public Drawing Process**

Step 1	The property is offered for sale at market value. Loan Servicer completes <i>Form 1955-40, Notice of Real Property for Sale</i> .
Step 2	The loan servicer advertises the property. Contacting known interested parties is part of advertising efforts. Program properties are offered exclusively to program applicants for the first 45 days, after which the property is available to anyone. The Agency may accept offers from program applicants prior to the advertised drawing date. Non-program purchase offers cannot be accepted prior to the drawing date.
Step 3	Offers are accepted and stamped with the date and time of receipt.
Step 4	Agency reviews offers. If only one offer is received and the offer meets Agency requirements that single offer may be accepted. If more than one offer is received the Agency will accept the offer which is in the best interest of the government. If acceptable offers are comparable, these will be sealed, placed in a receptacle and drawn sequentially.
Step 5	If no acceptable offer is received, reduce price by 10 percent or use other incentives. Repeat steps 1 through 4.
Step 6	If no acceptable offer, submit REO file with documentation of marketing efforts to State Office for further advice on sales incentives or to authorize sealed bid/auction. Loan Servicer may reevaluate whether the project should be classified as a program property.

A. Listing the Property

REO property is offered for sale using *Form RD 1955-40, Notice of Real Property for Sale*. The date indicated on *Form RD 1955-40* is the effective date of the offer. An offer may be submitted at any time after the effective date listed in the notice.

When an offer is accepted, the notice of sale is revised to indicate that only back-up offers will be taken. The notice is not withdrawn until the sale is closed, except when the offer is from a nonprofit organization or a public body for transitional housing for the homeless.

REO Property Subject to Redemption Rights

REO property subject to redemption rights may still be sold if field staff determines that there is no probability of its redemption and state law permits its sale. In states where such sales are permitted, a State Supplement will be issued with the specific state law requirements. The buyer must sign a statement acknowledging sale conditions under state law. The original signed statement will be filed in the REO file and transferred to the borrower's case file if it is Agency financed.

B. Submission Requirements

An offer to buy must be submitted on *Form RD 1955-45, Standard Sales Contract, Sale of Real Property of the United States*. Offers received in any other form must be returned to the offeror. Any offer to buy that is contingent upon Agency credit must be accompanied by a completed *Form SF 424.2, Application for Federal Assistance*. Applications are considered completed and acceptable only if they include the required attachments. To establish borrower eligibility, the following attachments must be included when the application is submitted:

- Financial statements (for past two years);
- Credit report for each general partner (if limited partnership) or each officer (if corporation);
- Proposed limited partnership agreement and certificates of limited partners (if applicable);
- Tax exempt ruling from the IRS designating the borrower organization as a 501(c) (3) or 501(c) (4) (if applicant is nonprofit). If designation is pending, a copy of the designation request;
- Mission statement;
- Evidence of organization under state and local law or copies of pending applications; and
- List of board members

Those requesting Agency credit must meet the applicant eligibility requirements as outlined in paragraph 5.11 of the Loan Origination Handbook.

C. Receiving and Considering Offers

Each offer must be date stamped when it is received. Offers received on the same day will be selected for consideration by lot. Names will be placed in a receptacle, drawn, and numbered sequentially. Offers drawn after the first are held as back-up and the offeror so notified.

The Agency selects the first minimum acceptable offer received and executes *Form RD 1955-45, Standard Sales Contract, Sale of Real Property of the United States*. The form is then sent to the bidder along with a letter to indicate acceptance of the offer. A letter is also sent to notify all unsuccessful bidders of the status of their offers.

D. Cancellation of Sales Contracts

If an offer contingent upon obtaining Agency financing on program terms is selected and the credit request is subsequently rejected, the next offer is considered. Property is not held off the market pending the outcome of an appeal. If there are no back-up offers, the notice of sale is revised to indicate the new status of the property.

When a sales contract is canceled due to offeror default, any earnest money collected is forwarded to the local Agency office where it will in turn be forwarded to the Finance Office for application to the General Fund.

14.19 DISPOSITION BY SEALED BID OR AUCTION

Any use of the sealed bid or auction methods must be authorized by the State Director. Program properties may be sold using these methods only after regular sales efforts have been unsuccessful for six months. Either method may be used as the initial sale effort for non-program properties when regular sale efforts are not likely to result in prompt sale (such as when structures have been substantially destroyed by fire).

A. Establishing the Minimum Acceptable Offer

Field staff must develop and document the recommendation for the minimum acceptable bid or sales price using the Net Recovery Value worksheet provided in Chapter 10, **Attachment 10-A**.

B. Publicizing the Sale

The Agency solicits sealed bids or publicizes an auction by public notice. The notice must include the date, time, and place of the bid opening or auction, describe how bids are to be made, the required percentage of bid deposit, the maximum credit terms, the cash preference percentage described in Paragraph C.3 below, and other pertinent information, such as a notice of special flood or mudslide hazard area or wetland and any related use restrictions.

C. Sealed Bid Procedures

1. Submission Requirements

Sealed bids must be made on *Form RD 1955-46, Invitation, Bid, and Acceptance, Sale of Real Property of the United States*, and be accompanied by a deposit provided in the form specified in the bidding instructions. No deposit is required from bidders who are eligible program purchasers. A minimum deposit of 10 percent is required for non-program loans.

Bidders must submit their bids in a sealed envelope marked: “SEALED BID OFFER _____*.” (*Insert “PROPERTY IDENTIFICATION NUMBER.”)

Bids may be submitted for individual properties or a group of properties.

2. Receiving and Opening Bids

All bids will be date and time stamped when they are received. Sealed bids will be held in a secured file before bid opening. The bid opening will be held publicly at the place and time specified in the notice with at least two Agency employees present. Each bid received will be recorded showing the name and address of the bidder, the amount of the bid, the amount and form of deposit, and any conditions of the bid. The record of bids will be signed by the staff person conducting the bid opening and retained in the REO file.

3. Reviewing and Accepting Bids

Only responsive bids will be considered. To be considered responsive, bids must be signed and dated by the offeror, include any required deposit, and be for an amount at least equal to the established minimum bid. Minor deviations or defects in the bid submission may be waived by the Approval Official so long as the bid meets these minimum requirements.

Generally, the highest bid will be selected. However, cash bids will be given preference over bids that are contingent upon the offeror obtaining financing if the cash offer is at least equal to a specified percentage of the highest offer. Exhibit B of RD Instruction 440.1, Interest Rates, Amortization, Guarantee Fee, Annual Charge, and Fixed Period, specifies the applicable percentage.

In the case of two identical bids for a program property, program-eligible purchasers will be selected before bidders who are not program-eligible.

4. No Acceptable Bid

If no acceptable bids are received, the Agency may negotiate a sale at the best price possible in accordance with paragraph 14.20. All bidders must be informed, in writing, of any anticipated negotiations. Deposits must be returned to all bidders by certified mail, return receipt requested.

5. Notification to Bidders

Field staff also must notify unsuccessful bidders in writing that their bids were not accepted and who the successful bidder was. Deposits must be returned to all unsuccessful bidders by certified mail, return receipt requested.

When a bid is accepted, field staff must execute *Form RD 1955-46, Invitation, Bid, and Acceptance, Sale of Real Property of the United States*, and send a written acceptance of the bid.

6. Failure to Close

If a successful bidder fails to perform under the terms of the offer, for any reason other than denial of credit by the Agency, the bid deposit will be forfeited and forwarded to the Finance Office for application to the General Fund.

Upon determination that the successful bidder will not close, the State Director may authorize direct negotiations with the next highest bidder, authorize another sealed bid sale, or authorize negotiations with other interested parties, as described in paragraph 14.20.

D. Auction Procedures

The State Director will determine whether an Agency employee will conduct the auction or whether the complexity of the sale requires the services of a professional auctioneer. *Form RD 1955-46, Invitation, Bid, and Acceptance, Sale of Real Property of the United States*, is used for auction sales.

1. Selecting a Professional Auctioneer

Auctioneers are selected through a competitive process using the procedures described in *RD Instruction 2024-A, Acquisition, Sales, and Leasing Authority*. The commission will be set as part of the auctioneer solicitation. If an auctioneer submits a bid with a commission rate that is significantly lower than other bids, detailed documentation will be provided attesting that they have successfully sold properties at the lower rate with no compromise in service.

2. Bid Deposits

Successful bidders will be required to make a bid deposit of 10 percent of the purchase offer. This fee will be waived for program-eligible bidders, pending final determination of eligibility. Deposits should be in the form of cashier's check, certified check, postal or bank money order, or bank draft payable to the Agency. Cash and/or personal check may be accepted only if deemed necessary for a successful auction to occur by the person conducting the auction.

Where program financing is authorized, all notices and publicity should provide for a method of prior approval of credit and the credit limit for potential program-eligible purchasers. This may include submission of letters of credit or financial statements prior to the auction. The auctioneer should not accept bids that request program financing in excess of the market value.

3. Accepting Bids

When the highest bid is lower than the minimum amount acceptable to the Agency, negotiations should be conducted with the highest bidder or, in turn, the next highest bidder(s) or other persons known to be interested in obtaining an executed bid at the predetermined minimum.

4. Purchaser's Default

Upon purchaser's default, the field staff will remit the bid deposit to the Finance Office as a Miscellaneous Collection. The property may then be disposed of through a negotiated sale.

14.20 NEGOTIATED SALE

If no acceptable bid is received either from a sealed bid sale or at a public auction, the State Director may negotiate a sale at the best price possible without further public notice by negotiating with interested parties, including previous bidders.

A sale made through negotiation will be documented and accepted by the Approval Official on *Form RD 1955-46, Invitation, Bid, and Acceptance, Sale of Real Property of the United States*, and must be accompanied by a bid deposit of 10 percent of the negotiated sales price, except that the deposit will be waived for program-eligible buyers.

14.21 DISPOSAL OF PROPERTY FOR SPECIAL PURPOSES

REO properties may benefit people in need of housing who can be reached in cooperation with other programs or Federal agencies. Cooperative agreements with other federal or state-assisted housing programs will be announced and updated with administrative notices.

14.22 DISPOSAL AS CHATTEL OR SALVAGE

If the Agency is unable to sell non-program property by regular sale, sealed bid or public auction, the structure may be sold as chattel or salvage to be removed from the site. *Form RD 1955-47, Bill of Sale 'A'*, is used to transfer title of real property converted to chattel to the purchaser.

If no offer is received to remove the structure, the State Director may contract or arrange to have it demolished, in exchange for the salvaged materials or otherwise as determined appropriate. For example, the local fire fighting unit may be permitted to use a structure slated for demolition as a burn for fire fighting practice. Once the structure is disposed of, the lot is offered for sale as non-program REO property.

If REO property is a vacant lot, the lot is offered for sale as non-program property.

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SECTION 3: ENVIRONMENTAL REQUIREMENTS

14.23 OVERVIEW

The Agency must complete the appropriate level of environmental review under the National Environmental Policy Act for disposal of REO property in accordance with RD Instruction 1940-G, Environmental Program. The proposed disposal of REO property will normally qualify as a categorical exclusion. However, an environmental assessment and an EIS (when deemed necessary) is required for any proposed disposal of REO property that meets one of the following criteria:

- The Agency has evidence that the transaction would result in a change in use of the REO property (e.g., the property is being sold as non-program and the application for Agency financing indicates that it will be used for commercial use;
- The transaction is controversial for environmental reasons;
- The property is located within a special flood or mudslide hazard area or contains a wetland;
- The property is located within the Coastal Barrier Resources System;
- The property is listed or eligible for listing on the National Register of Historic Places;
- The property contains reportable underground storage tanks; or
- The property is contaminated with hazardous substances or petroleum products.

This section summarizes the basic environmental information that pertains to disposal of REO properties. For more detailed information and assistance, refer to RD Instruction 1940-G, Environmental Program or consult the State Environmental Coordinator.

14.24 PROPERTY LOCATED WITHIN A SPECIAL FLOOD OR MUDSLIDE HAZARD AREA OR CONTAINS WETLANDS

REO property located in a special flood or mudslide hazard area will not be sold for residential purposes unless it is determined safe—that is, any danger that exists by virtue of the floodplain location is not likely to endanger the health or safety of the occupants—and prior written notice of the specific hazard is given.

Form RD 1955-46, Invitation, Bid, and Acceptance, Sale of Real Property of the United States, must include notice of special flood or mudslide hazard areas or wetlands and related use restrictions. Prospective purchasers, auctioneers, and brokers must be informed and acknowledge receipt of notice of these circumstances, and all advertisements need to reference them.

The conveyance instrument for disposal of REO property containing wetlands or located in a special flood or mudslide hazard area must specify those uses of the property that are restricted under any Federal, State or local floodplain and wetland regulations, as well as other relevant restrictions. Use restrictions will relate to the use of the property by the purchaser and any successors as determined by the Agency. Examples of use restrictions include prohibition of draining or filling of floodplain or wetland areas, prohibition of new above-ground construction on that portion of the property located in the floodplain or wetland area, and prohibition against subdividing floodplain or wetland property into building lots.

14.25 COASTAL BARRIER RESOURCES SYSTEMS

REO property located within a Coastal Barrier Resources System (CBRS) will not be sold until the State Environmental Coordinator has consulted with the appropriate Regional Director of the U.S. Fish and Wildlife Service, and the Regional Director concurs that the proposed sale does not violate the provisions of the Coastal Barrier Resources Act (CBRA).

No federal financing is permitted for REO property located within a CBRS, since flood insurance under the National Flood Insurance Program is not available for properties within the CBRS.

14.26 NATIONAL REGISTER OF HISTORIC PLACES

When REO property has been determined to be listed on (or eligible to be listed on) the National Historic Register, the Loan Approval Official responsible for conveyance must consult with the State Historic Preservation Officer (SHPO) in order to establish any necessary restrictions on the use of the property so that the future use will be compatible with preservation objectives as long as it does not result in an unreasonable economic burden to public or private interest. The Advisory Council on Historic Preservation must be consulted by the Loan Approval Official after the discussions with the SHPO are concluded.

Any restrictions that are developed on the use of the property as a result of the above consultations must be made known to potential bidders or purchasers through all advertisements and notices regarding the property, as well as in writing when the prospective purchaser signs the bid or offer to purchase. Acknowledgment of receipt of this notice will be obtained from the purchaser at that time and kept in the file.

14.27 PROTECTIVE COVENANTS AND EASEMENTS

The Agency has an affirmative responsibility to take actions to protect environmental resources located on REO property before that property is disposed of. “Affirmative responsibility” refers to the fact that there are certain protections that are required by federal, state, or local environmental laws. Frequently, such protective actions or mitigation measures will take the form of a covenant or conservation easement. In addition to floodplains, wetlands, coastal barriers, and historic places, this affirmative responsibility also extends to the following resources:

- Listed or proposed endangered or threatened species;

- Listed or proposed critical habitat;
- Designated or proposed wilderness areas;
- Designated or proposed wild or scenic rivers;
- Natural landmarks listed in the National Register of Natural Landmarks;
- Sole source aquifer recharge areas designated by EPA;
- Designated national trails;
- Important farmland; or
- Areas of high water quality.

The State Environmental Coordinator should be consulted if it appears that the proposed disposal of REO property may involve any of these resources.

14.28 REPORTABLE UNDERGROUND STORAGE TANKS

When disposing of REO property containing reportable underground storage tanks as described in paragraph 14.9 A.4 above, the Agency, if it has not already done so, must file the appropriate report with the State agency identified by the Environmental Protection Agency (EPA). The potential purchaser of the property will be informed by the Loan Approval Official of the reporting requirement and provided a copy of the filed report.

14.29 MANAGEMENT OF HAZARDOUS SUBSTANCES AND PETROLEUM PRODUCTS

All property considered for disposal must be evaluated for possible hazardous substance contamination. To do this, the Loan Approval official completes the *Transaction Screen Questionnaire, ASTM Standard E-1528 (TSQ)*, the initial level of inquiry in the due diligence process. (If a TSQ was completed prior to acquisition of the property, the Loan Approval Official must determine if the TSQ should be updated.) If the completed or updated TSQ indicates potential contamination, it will be sent promptly to the State Environmental Coordinator for further evaluation and guidance. All clean-up actions, if appropriate, will be taken under the guidance of the State Environmental Coordinator.

When leasing REO property, in whole or part, field staff must in all cases, notify potential lessees of the risk for potential contamination from hazardous substances, hazardous wastes, or petroleum products by providing the lessee with a copy of the agency's due diligence report on the property acquisition. The due diligence report should be accompanied by a written disclaimer to the effect that the agency does not provide any guarantee as to the accuracy of the report, but is simply making the results of its inquiry public.

A Covenant Regarding Hazardous Substance Remediation is provided as **Attachment 14-E**.

14.30 LEAD-BASED PAINT

The Agency must eliminate the hazards of lead-based paint poisoning in all REO properties before sale if they are to be used for residential purposes. Obligations include inspecting surfaces constructed prior to 1978 to determine whether there are defective paint surfaces, and treating surfaces found to contain lead-based paint to eliminate hazards. Prospective purchasers must be notified of the results of the inspection. **Appendix 5** includes specific guidance for addressing lead-based paint, and a sample disclosure format to provide purchasers with information about known lead-based paint hazards in the property.

SECTION 4: PROCESSING AND CLOSING

14.31 OVERVIEW

If the Agency is closing the sale with program financing, the sale is closed in accordance with program closing instructions provided in Chapter 9, Loan Closing and Project Lease-Up, of the Loan Origination Handbook. If other financing is being used, the financing agent's closing procedures should be followed. Cash sales are closed by the Agency collecting the sale price and delivering the Quitclaim Deed to the buyer.

Title clearance and property insurance requirements for a program-financed sale are the same as for a program loan.

14.32 SPECIAL NOTICES AT SALE

A. Disclosure of Lead-Based Paint or Hazards

In accordance with the Residential Lead-Based Paint Hazard Reduction Act of 1992, sellers of housing built before 1978 receiving federal assistance must provide the purchasers of such housing with specific information about the housing's lead history and general information on lead exposure prevention. As seller the Agency must:

- Provide the buyer with the lead hazard information pamphlet, Protect Your Family from Lead in Your Home, available from the National Lead Information Clearinghouse at 1-800-424-LEAD, or a similar EPA-approved pamphlet developed by the State;
- Permit the buyer a 10-day opportunity to conduct a risk assessment or inspection for the presence of lead-based paint hazard; and
- Include in the sales contract: (1) disclosure of any lead-based paint hazard or a statement that the Agency has no knowledge of such hazard; (2) a list of any information about the hazard available to the seller and passed on to the buyer; and (3) a Lead Warning Statement and acknowledgment, signed by the buyer. A sample disclosure format, including the required Lead Warning Statement, is provided in **Appendix 5**.

14.33 INSPECTION

An inspection of the property by the buyer should be scheduled immediately before closing to ensure satisfactory condition of the property and the resolution of any problems or discrepancies.

14.34 PRORATING REAL ESTATE TAXES AND/OR ASSESSMENTS

When REO property is subject to taxation and/or assessment, they are pro-rated between the Agency and the buyer, as of the date the title is conveyed. The Agency is responsible for all taxes and assessments accrued as of the settlement date, and the buyer is responsible for all taxes

and assessment which accrue after the closing date. The Agency's pro rata share is deducted from the proceeds of the sale at closing, if sufficient funds are available, or is paid under *RD Instruction 2024-A, Acquisition, Sales, and Leasing Authority*.

14.35 COMMISSIONS

Commissions are paid at closing if there is sufficient cash from sale proceeds to cover the commission. If not, the Agency will pay the commission and charge it to the REO account as a recoverable cost.

14.36 TRANSFERRING TITLE

The Agency conveys the property to the buyer by *Form RD 1955-49, Quitclaim Deed*, or other form of nonwarranty deed approved by OGC. The State Director signs the conveyance instrument, a copy of which is retained in the REO property case file. The buyer is responsible for recording the instrument.

14.37 REPORTING SALE

When the transaction is closed and the conveying instrument has been delivered, the disposition is recorded in the REO system. Real property that has been disposed of by means other than sale, including total loss or destruction, will also be reported in the REO System. Sale proceeds are forwarded to the Finance Office to be credited to the General Fund.

SECTION 5: PROCESSING CREDIT SALES ON NON-PROGRAM TERMS

14.38 OVERVIEW OF SECTION

The sale of non-program properties is conducted in a manner similar to other sales; however, there are some differences in the terms of the sale, the processing of the offers, loan closing, and the treatment of the property after the sale is complete. This section highlights these differences. (See the Loan Origination Handbook for processing credit sales for program properties.)

14.39 TERMS OF A NON-PROGRAM CREDIT SALE

The following provisions apply to credit sales on non-program terms.

- **Interest rate.** The Section 515 interest rate plus 0.5 percent will be charged on all types of housing credit sales. Refer to Exhibit B of RD Instruction 440.1, Interest Rates, Amortization, Guarantee Fee, Annual Charge, and Fixed Period (available in any Agency Office) for interest rates. Loans made on non-program terms will be equal to the lesser of the prevailing interest rate at the time of loan approval or loan closing.
- **Term of note.** The note amount will be amortized over a period not to exceed 10 years. If the State Director determines more favorable terms are necessary to facilitate the sale, the note amount may be amortized using a 30-year factor with payment in full (balloon payment) due not later than 10 years from the date of closing. In no case will the term be longer than the period for which the property will serve as adequate security.

14.40 ACCEPTING OFFERS

The sale of a non-program property is similar to other sales. Field staff publicize the sale, accept bids, and choose a bid from the first acceptable bids received.

- **Documenting offers and acceptance.** Field staff must use *Form RD 1955-45, Standard Sales Contract, Sale of Real Property of the United States* or *Form RD 1955-46, Invitation, Bid, and Acceptance, Sale of Real Property of the United States*, as appropriate, to document the offer and acceptance. Field staff must accept the contract prior to processing a request for credit on non-program terms.
- **Cash sales.** If the offerer can purchase the property without Agency assistance, field staff will simply collect the purchase price (less any deposits) and deliver the deed to the purchaser.
- **Purchase with non-program credit.** Purchasers requesting credit on non-program terms will be required to submit documentation to establish financial stability, repayment ability, and creditworthiness.

- ◇ The borrower may submit the standard forms used to process program applications or comparable documentation. Field staff may request additional information as needed to support loan approval.
- ◇ Field staff will order individual credit reports for each individual applicant and each principal within an applicant entity. Commercial credit reports will be ordered for profit corporations and partnerships, and organizations with a substantial interest in the applicant entity.

14.41 APPROVAL

field staff must use *Form RD 1944-51, Multi-Family Housing Obligation – Fund Analysis*, to approve a credit sale even though no obligation of funds is involved. For guidance on how to complete the form, see the special instructions on the FMI pertaining to non-program credit sales.

The Loan Servicer must review *Form RD 1910-11, Applicant Certification Federal Collection Policies for Consumer or Commercial Debts*, with the applicant, and the form must be signed by the applicant.

14.42 CLOSING SALE

The Loan Servicer will provide the closing agent with necessary information for closing the sale. Title clearance, loan closing, and property insurance requirements for a credit sale are similar to those for program loans. As for program sales, OGC assistance will be requested to provide closing instructions.

The following are the highlights of the closing process for non-program sales:

- **Closing costs.** The purchaser will pay his/her own closing costs. Earnest money, if any, will be used to pay purchaser's closing costs with any balance of closing costs being paid by the purchaser. Any closing costs which are legally or customarily paid by the seller will be paid by the Agency from the down payment.
- **Down payment.** A down payment of not less than 10 percent of the purchase price is required at closing and will be remitted by the field staff.
- **Modification of security instruments.** Field staff must modify security instruments as necessary.
 - ◇ On the promissory note and/or security instrument (mortgage or deed of trust) any covenants relating to graduation to other credit, restrictive-use provisions, personal occupancy, inability to secure other financing, and restrictions on leasing may be deleted.
 - ◇ Deletions are made by drawing a line through the specific inapplicable language. The borrower and an Agency representative must initial the changes.

- **Purchase of more than one property.** When more than one property is bought by the same buyer and the transactions are closed at the same time, a separate promissory note will be prepared for each property, but one mortgage will cover all the properties.
- **Reporting sale.** When the transaction is closed and the conveying instrument has been delivered, field staff will report the sale like all other sales. They will process *Form RD 1965-20, Multiple Family Housing Advice of Mortgaged Real Estate Sold*, in accordance with the respective FMI.

14.43 SERVICING THE NON-PROGRAM LOAN

Credit sales on non-program terms will be classified as non-program loans and serviced accordingly. The project is not subject to any rent, occupancy, or other program requirements.

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ATTACHMENT 14-A

**SAMPLE STATEMENT OF WORK
FOR PROPERTY MANAGEMENT CONTRACT**

(To be provided when developed)

ATTACHMENT 14-B
UNDERGROUND STORAGE TANKS
THAT MUST BE REPORTED

A. Underground storage tanks that meet the following criteria must be reported in two types of situations.

1. **Situation 1**

- A tank, or combination of tanks (including pipes which are connected thereto), of which the volume is 10 percent or more beneath the surface of the ground, including the volume of the underground pipes;
- The tank is not exempt from reporting requirements under Paragraph B below; and
- The tank contains petroleum or substances defined as hazardous under Section 101(14) of the Comprehensive Environmental Response Compensation and Liability Act, 42 U.S.C. 9601. The State Environmental Coordinator should be consulted whenever there is a question regarding the presence of a regulated substance.

2. **Situation 2.** It is known that the tank contained a regulated substance, was taken out of operation by the Agency since January 1, 1974, and remains in the ground. Extensive research of records of inventory property sold before the effective date of this section is not required.

B. Underground storage tanks that are exempt from the Environmental Protection Agency (EPA) reporting include:

- Farm or residential tanks of 1,100 gallons or less capacity used for storing motor fuel for noncommercial purposes;
- Tanks used for storing heating oil for consumptive use on the premises where stored;
- Septic tanks;
- Pipeline facilities (including gathering lines) regulated under: (1) the Natural Gas Pipeline Safety Act of 1968; (2) the Hazardous Liquid Pipeline Safety Act of 1979; or (3) for an intrastate pipeline facility, regulated under State laws comparable to the provisions of law referred to in (1) or (2);
- Surface impoundments, pits, ponds, or lagoons;

- Storm water or wastewater collection systems;
- Flow-through process tanks;
- Liquid traps or associated gathering lines directly related to oil or gas production and gathering operations; or
- Storage tanks situated in an underground area (such as a basement, cellar, mineworking, drift, shaft, or tunnel) if the tank is situated upon or above the surface of the floor.

Even if a storage tank does not need to be reported according to these criteria, if the Agency has reason to believe there has been a release of petroleum or other regulated substance from an underground storage tank on a real estate owned (REO) property, this incident must be reported to the appropriate State Agency and the State Environmental Coordinator, who will inform the State Office of the appropriate action to take.

ATTACHMENT 14-C

MEMORANDUM OF UNDERSTANDING
BETWEEN
UNITED STATES DEPARTMENT OF AGRICULTURE (USDA)
AND
DEPARTMENT OF HEALTH AND HUMAN SERVICES (HHS)

ATTACHMENT 14-D

**MEMORANDUM OF UNDERSTANDING
BETWEEN THE
FEDERAL EMERGENCY MANAGEMENT AGENCY
AND THE
FARMERS HOME ADMINISTRATION**

PURPOSE

This Memorandum of Understanding establishes authorities and procedures whereby the Federal Emergency Management Agency (FEMA) may utilize both single family and multiple housing units which are habitable, and to which Rural Housing Service (RHS), an Agency of the U.S. Department of Agriculture (USDA), has title and possession. The housing units assigned to FEMA by RHS are to provide temporary housing to victims of major disasters or emergencies declared by the President, in accordance with Sections 302(a) and 404(a) of Public law 93-288, the Disaster Relief Act of 1974.

EFFECTIVE DATE OF THIS MEMORANDUM

This memorandum shall be effective on the date of the last signature hereto.

DURATION OF AGREEMENT

This memorandum shall continue to be in effect for a period coinciding with the authority under which it is entered.

MODIFICATIONS

This Memorandum of Understanding and its attachments may be modified in writing by mutual consent of the parties.

RESPONSIBILITIES

RHS shall make available to FEMA on request habitable single family and multiple housing units in its inventory that are located in designated disaster areas and that are not under lease or under agreement of sale. FEMA will reimburse RHS for authorized expenses, as set out herein, resulting from utilization of assigned housing units.

IMPLEMENTATION

This memorandum shall be implemented in accordance with the following general procedures. FEMA and/or RHS may prepare other detailed operating procedures as necessary for internal use of the agencies. These latter procedures will be in compliance with the provisions of this Memorandum.

- (a) Delegation of Authority. The signatories to this agreement will delegate authority to implement this agreement to their respective employees, in writing. When a disaster occurs, the persons to whom this authority has been delegated shall identify employees, contractors, and agents authorized to implement the appropriate provisions of this Memorandum of Understanding and other FEMA and/or RHS detailed operating procedures. FEMA and RHS will exchange a list containing names, addresses, and telephone numbers of such employees, contractors, and agents, who will implement the agreement with respect to the specific major disaster. Other references to FEMA and RHS in the following paragraphs will be interpreted to include contractors, agents, and employees designated to implement the provisions of this Memorandum of Understanding.
- (b) Assignment of RHS Housing Units to FEMA
 - (1) Upon declaration by the President of a major disaster or emergency, FEMA may request from the appropriate RHS State Director a list of all habitable housing units available in designated disaster areas indicating the county or counties where housing is needed.
 - (2) At its discretion, RHS may sell or lease units directly to displaced RHS borrowers instead of providing them to FEMA. RHS will provide FEMA a list of such sales or leases for information purposes and to prevent duplication of benefits.
 - (3) During the period of occupancy of a housing unit by a disaster victim, FEMA will inform the occupant that RHS lending assistance may be available for purchase of the housing unit as permanent housing.
 - (4) Before assignment to FEMA and occupancy by a disaster victim, each housing unit under consideration will be inspected jointly by RHS and FEMA. The agencies will then execute a Letter of Assignment for each habitable housing unit assigned to FEMA. A Pre-Occupancy and Termination Joint Inspection report (FEMA 90-11) will be prepared, signed by both agencies, and attached to the letter of assignment. The RHS advice number will be noted prominently on this form.
 - (5) RHS will remove all RHS signs, such as "no trespassing," "for sale," etc., from housing units assigned to FEMA.

MANAGEMENT OF HOUSING UNITS

- (a) Necessary maintenance on housing units assigned to FEMA shall be performed by FEMA at its expense, or FEMA shall reimburse RHS for accomplishing such maintenance as agreed upon by local agency representatives.
- (b) FEMA shall furnish to RHS the names and mailing addresses of unit occupants, the property designation, the beginning occupancy date, and notice of changes in occupancy.
- (c) During business hours RHS authorized employees may inspect housing units. Advance notice of forty-eight (48) hours will be given to FEMA, who will, in turn, advise the occupant.
- (d) FEMA shall not permit a disaster victim to occupy a housing unit beyond the period of eligibility in accordance with 44 CFR 205.52.
- (e) There shall be no rental charge to FEMA by RHS for assigned housing units for the first twelve (12) months from the date of the letter of assignment. If a housing unit is assigned to FEMA for more than one year after the date of the letter of assignment, FEMA shall pay RHS the fair market rental value as determined by RHS for each subsequent month.
- (f) If an occupant fails to vacate a housing unit after housing benefits are terminated, FEMA shall conduct the predetermination procedures in 44 CFR 205.52 and shall, if appropriate, undertake eviction action.

RETURN OF HOUSING UNITS TO RHS

- (a) When a housing unit is vacated and FEMA determines that it is no longer needed, FEMA shall notify RHS.
- (b) FEMA and RHS authorized employees, contractors, or agents will jointly inspect the vacated housing unit to determine maintenance, cleanup, and repairs required to return the housing unit to a physical condition comparable to that existing at the time of the initial joint inspection. Necessary maintenance and repairs shall be performed by FEMA at its expense, or FEMA shall reimburse RHS for accomplishing such repairs as agreed upon by local agency representatives. Repairs shall be made in accordance with local, state, or federal codes.
- (c) FEMA shall return the keys, custody of, and responsibility for units, to RHS when needed maintenance, cleanup, and repairs are completed. RHS shall prepare a receipt and provide a copy to FEMA.

APPROVALS

This agreement is executed by the Administrator, Rural Housing Service, USDA, and the Associate Director, State and Local Programs and Support, FEMA, by virtue of their general authorities to do so.

Administrator
Rural Housing Service
U.S. Department of Agriculture

Date: _____

Associate Director
State and Local Programs and Support
Federal Emergency Management Agency

Date: _____

**FEDERAL EMERGENCY MANAGEMENT AGENCY
and the
RURAL HOUSING SERVICE
FEMA-RHS LETTER OF ASSIGNMENT**

STATE: _____

COUNTY: _____

Under the Memorandum of Understanding between the Federal Emergency Management Agency (FEMA) and the Farmers Home Administration (now the Rural Housing Service [RHS]), effective November 3, 1982, the habitable housing unit identified on the attached inspection report is made available by RHS for use by FEMA or its Agent as temporary housing for victim(s) located within the following described designated disaster area and who are eligible for such assistance under the provisions of the Disaster Relief Act of 1974:

This Letter of Assignment shall become effective on the date signed by the authorized employees, contractors, or agents. This assignment is for the housing unit identified by the attached inspection report and having the following RHS advice number:

_____.

FEMA

RHS

NAME: _____

TITLE: _____

DATE: _____

ATTACHMENT 14-E
COVENANT REGARDING
HAZARDOUS SUBSTANCE REMEDIATION

- (1) The United States, acting through the (Agency name), warrants that all remedial action necessary to protect human health and the environment with respect to any such substance remaining on the property herein leased, transferred, or conveyed has been taken before the date of this lease, transfer or conveyance.
- (2) If lessor or transferee finds that additional remedial action is necessary to protect the human health and the environment after the date of this lease, transfer or conveyance, the United States, acting through the (Agency name), will conduct such action.
- (3) The hazardous substance remediation requirements described herein do not apply when the property is leased, transferred, or conveyed to a potentially responsible party.
- (4) The lessee or transferee herein, hereby grants to the United States, acting through the (Agency name), access to the property in any case in which remedial or corrective action is found to be necessary.

Note: If the lessee or transferee is a potentially responsible party (PRP), the Notification: Hazardous Substance Activity must be given, but the Covenant Regarding Hazardous Substance Remediation (**Attachment 14-E**) does not need to be included with the transfer.